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SUBJECT: SERBIA: 2008-2009 INCSR II ON MONEY LAUNDERING

REF: State 103813

SUMMARY  
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¶1. Reftel requested post update for Serbia on efforts to combat money laundering and terrorist financing. Serbia is upholding its international commitments to eliminate money laundering and terrorist financing. END SUMMARY.

BEGIN INCSR II TEXT

Serbia: Not a Financial Center  
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¶2. Serbia is not a regional financial center. At the crossroads of Europe and on the major trade corridor known as the "Balkan Route," Serbia confronts narcotics trafficking, smuggling of persons, drugs, weapons and pirated goods, money laundering, and other criminal activities. Serbia continues to be a significant black market for smuggled goods. Illegal proceeds are generated from drug trafficking, corruption, tax evasion and organized crime, as well as other types of crimes. Proceeds from illegal activities are invested in all forms of real estate. Trade-based money laundering (TBML), in the form of over- and under-invoicing, is commonly used to launder money. There are reports that the purchase of some private and state-owned companies was linked to money laundering activity.

¶3. A significant volume of money flows to Cyprus, reportedly as payment for goods and services. The records maintained by various government entities vary significantly on the volume and value of imports from Cyprus. According to Government of the Republic of Serbia (GOS) officials, much of the difference is due to payments made to accounts in Cyprus for goods, such as Russian oil, that actually originate in a third jurisdiction. Banks in Macedonia, Hungary, Switzerland, Austria and China have emerged as destinations for laundered funds.

Banking Sector Largely Foreign Owned  
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¶4. Serbia's banking sector is more than 80 percent foreign-owned. There is no provision in the banking law that allows the establishment of offshore banks, shell companies or trusts. Serbia has three designated operating free trade zones, established to attract investment by providing tax-free areas to companies operating within them. These companies are subject to the same supervision as other businesses in the country. There is no evidence of alternative remittance systems operating in the country. Nor is there evidence of financial institutions engaging in currency transactions involving international narcotics trafficking proceeds.

Anti-Money Laundering Law  
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¶5. Serbia's definition of money laundering in the Penal Code aims to conform to international standards. This legislation also gives police and prosecutors more flexibility to pursue money laundering charges. The penalty for money laundering is a maximum of 10 years imprisonment. Under this law and attendant procedure, money laundering falls into the serious crime category and permits the use of Mutual Legal Assistance (MLA) procedures to obtain information from abroad.

¶6. Under Serbia's anti-money laundering law (AMLL), entities must report suspicious transactions in any amount to the FIU. The law defines those sectors subject to reporting and record keeping requirements, including attorneys, auditors, tax advisors and accountants, currency exchanges, insurance companies, casinos, securities brokers, dealers in high value goods, real estate agencies, and travel agents, among those required to comply with the AMLL provisions. The AMLL requires entities to collect certain information and file currency transaction reports (CTRs) with the financial intelligence unit (FIU) on all cash transactions exceeding 15,000 euros (approximately U.S. \$19,000), or the dinar equivalent. These entities must also retain records for five years. Financial institutions improved their compliance, i.e., gathering and keeping records on customers and transactions. The AMLL requires obligated entities and individuals to monitor customers' accounts when they suspect money laundering, in addition to reporting to the FIU. Safe harbor provisions protect the entities with respect to their cooperation with law enforcement. The flow of information to the FIU has steadily increased, but not all entities are subject to implementing bylaws. The AMLL also eliminates a previous provision limiting prosecution to crimes committed within Serbian territory.

#### Law on Foreign Exchange

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¶7. The Law on Foreign Exchange Operations, adopted in 2006, criminalizes the use of false or inflated invoices or documents to conceal the illicit transfer of funds out of the country. Serbia enacted this law in part to counter the perceived problem of import-export fraud and TBML. The Foreign Currency Inspectorate, part of the Ministry of Finance, is responsible for supervising import/export companies for compliance. The law also requires residents and nonresidents to declare to Customs authorities all currency (foreign or dinars) and/or securities exceeding 5,000 euros (approximately U.S. \$6,500) transported across the border.

¶8. The National Bank of Serbia (NBS) has supervisory authority over banks, currency exchanges, insurance and leasing companies. The NBS has issued regulations requiring banks to have compliance and know-your-customer (KYC) programs in place and to identify the beneficial owners of new accounts. In June 2006, the NBS expanded its customer identification and record keeping rules by adopting new regulations mandating enhanced due diligence procedures for certain high-risk customers and politically exposed persons. The NBS developed similar regulations for insurance companies in 2006. The Law on Banks includes a provision allowing the NBS to revoke a bank's license for activities related to, among other things, money laundering and terrorist financing, but the NBS has not yet used this revocation authority. Although the legal framework is in place, the NBS currently lacks the expertise needed for effective bank supervision of money laundering, but is building these capacities through training and staff development.

¶9. The Securities Commission (SC) supervises broker-dealers and investment funds and monitors its obligors' compliance with the AML Laws. The SC is developing regulations to implement this authority.

The Law on Investment Funds and the Law on Securities and Other Financial Instruments Market provide the SC with the authority to "examine" the source of investment capital during licensing procedures.

#### Tax Administration

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¶10. Serbia's Tax Administration lacks the audit and investigative capacity and resources to investigate adequately the large number of suspicious transactions that are forwarded by Serbia's FIU. In addition, current tax law sets a low threshold for auditing purposes and has increased the burden on the Tax Administration. This has

created a situation where criminals can spend and invest illegal proceeds freely with little fear of challenge by tax authorities or other law enforcement agencies.

#### Financial Intelligence Unit in Place

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¶11. The Administration for the Prevention of Money Laundering (APML) serves as Serbia's FIU, with the status of an administrative body under the Ministry of Finance. APML has its own line-item operating budget. The FIU has developed listings of suspicious activity for banks, currency exchange offices, insurance companies, securities brokers and leasing companies. APML also has the authority to freeze transactions for 72 hours. The FIU signed memoranda of understanding (MOU) on the exchange of information with the NBS and Customs. The FIU authored Serbia's first National Strategy on Combating Money Laundering and Terrorist Financing, which the Government adopted in September 2008.

#### Recent Results

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¶12. From January 1, 2008, through November 05, 2008, the FIU received 2,087 suspicious transaction reports (STRs). The majority of the STRs received by the FIU were filed by commercial banks. In 2008, the FIU opened 31 cases. The public prosecutor's office reports 66 persons suspected of money laundering, with 33 requests for investigation and 27 issued and pending indictments.

¶13. In Serbia, it is difficult to convict a suspect of money laundering without a conviction for the predicate crime. The most common predicate crime is "abuse of office." To date, there have been three convictions. In addition, courts are unwilling to accept circumstantial evidence to support money laundering or tax evasion charges. This hampers law enforcement and prosecutorial authorities from effectively using the anti-money laundering laws. The Suppression of Organized Crime Service (SOCS) of the Ministry of Interior houses an Anti-Money Laundering Section to counter these challenges and focus financial investigations. Prosecutors' offices have assigned anti-money laundering liaison officers to ensure information sharing with the FIU. In October 2008, Serbia passed the Law on Asset Forfeiture which allows for asset sharing under separate international agreements.

#### Interagency Working Group Established

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¶14. The GOS has established the Permanent Coordinating Group (PCG), an interagency working group originally tasked with developing an implementation plan for the recommendations from the Council of Europe Select Committee of Experts on the Evaluation of Anti-Money Laundering Measures' (MONEYVAL) first-round evaluation. Subgroups have since worked to draft amendments to the AMLL that will bring the country's laws into compliance with the European Union's Third Directive on money laundering. The PCG and the working groups meet intermittently as required for completing specific tasks. However, the GOS still lacks consistent interagency coordination.

¶15. Under the law, the GOS can, upon conviction for an offense, confiscate assets derived from criminal activity or suspected of involvement in terrorist financing. The FIU enforces the United Nations Security Council Resolution (UNSCR) 1267 provisions regarding suspected terrorist lists. Although the FIU routinely provides the UN list of suspected terrorist organizations to the banking community, examinations for suspect accounts have revealed no evidence of terrorist financing within the banking system. The SOCS, the Special Anti-Terrorist Unit (SAJ), and Gendarmerie in the Ministry of Interior are the law enforcement bodies responsible for planning and conducting the most complex antiterrorism operations. SOCS cooperates and shares information with its counterpart agencies in countries bordering Serbia. Although Serbia has criminalized the financing of terrorism - penalties include the freezing, seizing and confiscation of assets of terrorists in accordance with UN Security Council resolutions - it still lacks a legal basis, pending enactment of draft anti-terrorism finance legislation. This draft law on terrorist financing, now pending Parliamentary approval, will apply all provisions of the AMLL to terrorist financing; require reporting to the FIU of transactions suspected to be terrorist financing; and will create mechanisms for freezing, seizing and

confiscating suspected terrorist assets based on UNSCR provisions.

#### Cooperation with Others

¶16. Serbia has no laws governing its cooperation with other governments related to narcotics, terrorism, or terrorist financing. Bases for cooperation include participation in Interpol, bilateral or regional cooperation agreements, and agreements concerning international legal assistance. There are no laws governing the sharing of confiscated assets with other countries.

¶17. Serbia does not have a mutual legal assistance arrangement with the United States, but information exchange via a letter rogatory is standard. The 1902 extradition treaty between the Republic of Serbia and the United States remains in force. The treaty allows the Serbian government to extradite non-Serbs to the United States. The GOS has bilateral agreements on mutual legal assistance with 31 countries. As a member of MONEYVAL, Serbia will undergo a mutual evaluation in 2009. The FIU is a member of the Egmont Group and participates in information exchanges with counterpart FIUs including FinCEN. APML has also signed information sharing memoranda of understanding (MOUs) with eleven counterpart FIUs.

¶18. Serbia is a party to the 1988 UN Drug Convention, the UN Convention against Corruption, and the UN Convention Against Transnational Organized Crime. The GOS also is a party to all 12 UN Conventions and protocols dealing with terrorism, including the UN International Convention for the Suppression of the Financing of Terrorism. Domestic implementation procedures, however, do not provide the framework for full application of Convention provisions.

#### Next Steps

¶19. Serbia should continue to work toward eliminating the abuses of office and the culture of corruption that enables money laundering and financial crimes. The GOS should take action to realize and implement the pending legislative initiatives necessary for Serbia to comply fully with international standards. These include the laws providing for the liability of legal persons and regulations applying all requirements of the AMLL to cover nonbank financial institutions. The GOS should enforce anti-money laundering regulations pertaining to money service businesses and obligated nonfinancial business and professions. Serbia should complete its supervisory scheme and enact binding regulations for the securities sectors. Serbia also needs to enact and implement legislation needed to comply with UN Security Council resolutions regarding the freezing, seizing and confiscation of suspected terrorist assets and to require suspicions of terrorist financing to be reported to the FIU. The National Bank and other supervisory bodies need to enhance their knowledge and resources. On an operational level, law enforcement needs audit and investigative capacity to investigate the STRs that the FIU disseminates. Prosecutors and judges also need a better understanding of money laundering and terrorist financing to ensure successful prosecutions. Rather than address specific tasks as an ad hoc group, the PCG should meet on a regular basis to discuss issues and projects and work to improve interagency coordination in such areas as information sharing, record keeping, and statistics.

END INCSR II TEXT

#### Comment

¶20. Serbia is upholding its international commitments to eliminate money laundering and terrorist financing. Serbia continues to strengthen its anti-money laundering and terrorist financing law enforcement with the help of the U.S Department of Justice, which provides training in organized crime investigation, prosecution, and adjudication. Although key legislation is still needed, Serbia has made progress, as evidenced by the adoption of the Law on Asset Forfeiture. END COMMENT.

MUNTER